

**TO: THE CHIEF EXECUTIVE OR MANAGING OFFICER OF ALL LOUISIANA  
STATE-CHARTERED CREDIT UNIONS**

**FROM: SID SEYMOUR, CHIEF EXAMINER**

**DATE: NOVEMBER 9, 2007**

**RE: LOUISIANA OFFICE OF FINANCIAL INSTITUTIONS (OFI) - UPDATE**

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**Outreach Initiative** – Earlier this year, Commissioner John Ducrest, Deputy Chief Examiner John Fields, and I visited with a number of you to discuss regulatory trends and stress the importance of credit unions serving the economic needs of their members. We asked what are the greatest challenges to remaining small, independent, credit unions. The comments we most often heard included: increased competition; heavy regulatory burden; shrinking net interest margins; difficulties in hiring and retaining competent staff; and difficulties in attracting new, and younger volunteers to serve as directors and committee members. While we support reduced regulatory burden, we encourage you to look upon this Office as not only a regulatory agency but also a resource. While everyone seems to agree that the credit union industry has become increasingly more complicated and competitive, key performance indicators remain strong and reflect favorably on management of the credit unions domiciled in the State of Louisiana. We recognize your continued efforts in this regard.

**New Initiatives** – This Office continues to strive to be a valuable resource to your credit union by being proactive, knowledgeable, and a responsive to your needs. Beginning in 2008, the following new initiatives will be implemented in order to reduce the regulatory burden on state-chartered credit unions:

- (1) Examination frequency- This Office will be moving out its examination frequency for 1- and 2-rated credit unions to approximately 18 months. These credit unions will generally be well-capitalized, well-managed, staffed by more than one full-time employee, and have total assets of less than \$25 million. Since the re-shuffling of our schedules may present conflicts, it may not be possible to move all of these examinations out to 18 months immediately, but we will do our best to keep the examinations of the strongest credit unions out to the furthest extent.
- (2) More examination report review in field- This Office has successfully completed the first phase of having its examination reports of our credit unions that are 1- rated with less than \$25 million in total assets completed in our district offices and mailed directly to you. Now, we will add the 2-rated credit unions to this list. We are hopeful that this initiative will reduce the time between the examiners' completion of an examination and the time that it takes for you to get the final examination report. We realize that the quicker we can get the information back to you, the sooner you can start working on correcting any deficiencies. However, credit unions with a 3-rated management; total assets greater than \$25 million; or currently operating under some form of enforcement action will continue to be processed in the Main Office.

**Overall Financial Condition** -- A vast majority of our state-chartered credit unions remain in sound financial condition. As of June 30, 2007, there were 49 state-chartered credit unions in Louisiana. As of June 30, 2007, 94% had a composite CAMEL rating of 1 or 2, compared to 89% as of June 30, 2006. Credit unions experienced upgrades primarily in the asset quality and liquidity components. While examination results for those credit unions significantly affected by Hurricanes Katrina and Rita continue to be generally favorable, the short-term economic impact on earnings and liquidity (as a result of the significant outflow of hurricane-related funds) is an area of concern that we will continue to monitor very closely.

The following chart contains CAMEL rating information for ALL credit unions domiciled in the State of Louisiana.

**CAMEL Ratings for All Credit Unions domiciled in Louisiana @ 6/30/07**

<b>Composite CAMEL</b>	<b>All CU's %</b>	<b>State CU's %</b>	<b>Federal CU's %</b>
Rating of "1"	49 20%	22 45%	27 14%
Rating of "2"	126 53%	24 49%	102 54%
Rating of "3"	53 22%	3 6%	50 26%
Rating of "4"	11 5%	0 0%	11 6%
Rating of "5"	0 0%	0 0%	0 0%
Not Yet Rated	0 0%	0 0%	0 0%
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TOTAL	239	49	190
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**2007 Legislative Fiscal Session** – All three of the OFI bills that were introduced during the recent Legislative Fiscal Session were passed and signed by the Governor. One bill in particular, HB 314 (Act 36) established an online licensing system for our licensees under the Residential Mortgage Lending Program that will greatly assist state agencies nationwide in detecting and preventing mortgage loan fraud. If you want more information about this online database, please contact Deputy Chief Examiner Darin Domingue at 225/922-2596 or by email at [ddomingue@ofi.louisiana.gov](mailto:ddomingue@ofi.louisiana.gov). The enrolled bills are available on the Legislature's website at: [www.legis.state.la.us](http://www.legis.state.la.us). Please contact General Counsel Sue Rouprich at 225/922-1028 or by email at [srouprich@ofi.louisiana.gov](mailto:srouprich@ofi.louisiana.gov) with any questions. We are currently considering legislation for the upcoming 2008 Legislative Regular Session and will be meeting with the LCUL in the very near future to discuss our legislative package.

**Residential Group Common Bonds and Associational Groups** – This rule, which became final on **August 20, 2007**, establishes the criteria to be used by state-chartered credit unions filing an application for a residential group common bond within a well-defined neighborhood, small community, or rural district; and adding associational groups. Please note that the Louisiana Credit Union Law currently allows only those individuals that **reside** within a well-defined neighborhood, small community, or rural district to join the credit union. We are hopeful that the geographic expansion authority in the final rule, coupled with the ability to **retain** your existing field of membership, the authority to establish maximum interest rates that **can** exceed those of federally-chartered credit unions, the benefit of local supervision, OFI's nationally-recognized accreditation through the National Association of State Credit Union Supervisors (NASCUS), and broad parity statutes, will improve the attractiveness of the state charter. Please contact Deputy Chief Examiner John Fields at (225) 922-0633, [jfields@ofi.louisiana.gov](mailto:jfields@ofi.louisiana.gov) with any questions regarding the filing of such an application.

**Unrelated Business Income Tax Update** – The National Association of State Credit Union Supervisors (NASCUS) has continued its efforts to challenge the Internal Revenue Service (IRS) on its interpretation of what income, if any, earned by state-chartered credit unions should be subject to federal taxation under the provisions of the Internal Revenue Code (IRC) Section 511-513. This section declares that certain tax-

exempt organizations under IRC Section 501(c) must pay federal income tax on net income realized from sources that are not substantially related to the tax exempt purpose of the organization. Such income is deemed “unrelated business income” and, therefore, taxable.

As of June 22, 2007, a total of 25 Technical Advice Memoranda (TAMs) have been released and made public by the Internal Revenue Service on unrelated business income tax (UBIT). The IRS has determined in its recent TAMs that interchange income derived from VISA credit cards and checkcard programs is related to the tax exempt purposes of a credit union, and therefore not subject to UBIT.

While this Office and NASCUS are in agreement that these products/services are consistent with credit unions’ tax exempt purposes, the IRS has determined that net income derived from the following products/services should be subject to federal taxation:

- Sale of accidental death and dismemberment (AD&D) insurance;
- Sale of group life, dental, health and cancer insurance;
- Car buying service and sale of car warranties;
- Sale of guaranteed auto protection (GAP) insurance;
- Sale of credit life and disability insurance;
- Sale of MEMBERS financial management services; and
- Fees from nonmember ATM usage.

Additionally, the IRS has determined that the following services are not subject to UBIT:

- Sale of checks;
- Collateral protection insurance;
- Interchange income from VISA credit cards and checkcard programs

While the TAMs do not set a precedent for all state-chartered credit unions, they could indicate how an IRS auditor may treat a state-chartered credit union in this regard. Because products, services, and pricing structures are unique to individual credit unions, each credit union should work closely with its CPA firm in making any decisions related to UBIT for 2007 and 2008.

You are reminded that appropriate expense allocation **will reduce** the amount of income that is subject to taxation. If a credit union does not track specific cost centers for such items, it may be allowed to determine the amounts on a pro-rata basis, using the percentage that the unrelated business income represents of the credit union’s gross income and net “pro-rata” expenses against the said income. Credit unions should consult with their CPAs/Auditors about Form 990T and seek advice regarding how to calculate the income and expenses relating to UBIT. Please contact Deputy Chief Examiner Fields if you want copies of the TAMs, or with any questions.

**Filing of IRS Form 990** - Historically, the OFI has filed a joint Form 990 for all Louisiana state-chartered credit unions. This serves as official notification that the OFI will no longer be filing the Internal Revenue Service (IRS) Form 990 tax return beginning with the 2007 tax year. While the Form 990 was an informational return for non-profit entities, the Form 990-T includes the calculation of a possible Unrelated Business Income Tax (UBIT). The OFI is not prepared to provide accounting or legal advice regarding UBIT. The tax forms are due to the IRS by **May 15, 2008**; however, non-profit entities are allowed to also file for an automatic 3-month extension with the completion and submission of a **Form 8868** to the IRS prior to the due date.

We will hold workshops in various areas of the state or conference calls to “walk” credit unions through the process of filling out and filing Form 990 returns. The workshops will be scheduled in sufficient time for credit unions to file their returns by the due date. The Louisiana Credit Union League (LCUL) has requested that they be advised of the dates, times and places of these workshops in order to publicize them, in addition to any information sent out by this Office. NASCUS is also looking at offering an online webinar on this topic at year-end or January 2008. We urge all of you to make plans to participate in one of the workshops. Again, please contact Deputy Chief Examiner Fields for more details.

**Congressional Data Collection Initiative** – In 2006, the House Ways and Means Committee began looking into how consumers benefit from credit unions’ tax-exempt status. As a result, the NCUA collected this data in a representative sampling that included 448 federal credit unions nationwide and issued its report on November 15, 2006. The NCUA indicated the following regarding the data it collected:

- 60% of the membership in the average federal credit union has a median family income of less than \$60,000 annually
- 82% has less than \$75,000, and
- 96% has a median family income of less than \$100,000.

OFI participated in a similar initiative coordinated by NASCUS and collected data in order to prepare a similar report for the Committee on state-chartered credit unions. Five (5) state-chartered credit unions domiciled here in Louisiana were randomly selected to be included in the data collection initiative. The process included the use of a questionnaire and geocoding software to respond to questions concerning the following areas: income characteristics of members; executive compensation; unrelated business income; and CUSOs. We have completed the data collection process and submitted it to NASCUS for processing. NASCUS is processing the data and preparing the final report. NASCUS has set a goal to have its final report prepared for the Committee by year-end 2007 due to delays in obtaining data from some of the other participating states. Please contact Deputy Chief Examiner Fields with any questions.

**Information on the NASCUS Website** – You are again encouraged to periodically check the NASCUS website at <http://www.nascus.org> for information and updates on the most current matters affecting state-chartered credit unions. The Regulatory Affairs Section (<http://www.nascus.org/regulatory.html>) contains details on proposed rules and requests for comments that may affect state-chartered credit unions. The Legislative Affairs Section (<http://www.nascus.org/legislative.html>) provides information and NASCUS’ commentary on proposed federal legislation that may affect state-chartered credit unions. Generally, NASCUS comments only on federal legislation that may affect the dual chartering system, state-chartered credit unions, share insurance requirements, or infringe upon state regulatory authority. Please contact Deputy Chief Examiner Fields with any questions regarding NASCUS, its website, accessing the information, or understanding the purpose and intent of the various issuances and/or proposals.

**Recent Examination Topics of Interest** – Examiners continue to see situations where management has obtained sample policies and procedures from third-parties. Upon closer review, it’s obvious that management has simply added the credit union’s name to the policies and procedures. Although it’s a pretty common practice, the Board of Directors, along with management, is ultimately responsible for ensuring that any new policies and procedures meet the unique needs of the credit union and its members. Please contact Deputy Chief Examiner Fields with any questions.

**Visa Stock** – Recently, the NCUA issued a legal opinion that said federal credit unions may accept and hold Visa stock in connection with Visa's conversion to public ownership. Visa U.S.A. will become a subsidiary of Visa, Inc., as part of its restructuring, and Visa member institutions will receive stock in Visa, Inc., calculated on the basis of fees it has generated. Member institutions will not compensate Visa, Inc., for the stock, and will receive the stock without taking any further action, and no cash or other rewards to members are available in lieu of the stock. Generally, the Federal Credit Union Act does not authorize federal credit unions to invest in any companies other than CUSOs. While Visa is not a CUSO, NCUA indicated that federal credit unions may receive and retain the Visa stock because it is a by-product of lending, which is a permissible activity for federal credit unions, and does not require federal credit unions to invest in an otherwise impermissible investment.

NCUA also cautioned that federal credit unions may receive and retain the stock unless the examiner determines that holding the stock is a safety and soundness problem for the credit union. NCUA said that state chartered credit unions should get an opinion from the state supervisory agency on this issue. The LCUL requested such an opinion from this Office.

Pursuant to LSA – R. S. 6:667.1(B) of the Louisiana Credit Union Law, we have determined that it would be appropriate to allow state credit unions in Louisiana to receive and retain such stock under the same rationale and conditions that apply to federal credit unions. Please contact me directly with any questions.

**Closing Comments** – Please accept my sincere appreciation of your continued support of this Office, and know that we are always looking for ways to improve the manner in which we assist you. If you have noticed an area in which we are not excelling, regardless of whether it has always been that way, please let me know. You can call me directly at 225-925-4675, or email [sseymour@ofl.louisiana.gov](mailto:sseymour@ofl.louisiana.gov). We can't do better if we don't know better!